BELLSOUTH

**BellSouth Telecommunications, Inc.**
601 W. Chestnut Street
Room 407
Louisville, KY 40203

Dorothy.Chambers@BellSouth.com

**Dorothy J. Chambers**
General Counsel/Kentucky

502 582 8219
Fax 502 582 1573

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Drop Box



Mr. Thomas M. Dorman
Executive Director
Public Service Commission
211 Sower Boulevard
P. O. Box 615
Frankfort, KY 40602

Re: The Review of BellSouth Telecommunications, Inc.'s Price Regulation Plan
PSC 2003-00304

Dear Mr. Dorman:

Enclosed for filing in the above-captioned case are the original and ten (10) copies of BellSouth Telecommunications, Inc.'s Response to Comments of AT&T of the South Central States, LLC, MCI WorldCom Communications, Inc. and the Kentucky Attorney General.

Very truly yours,

Dorothy J. Chambers

Enclosure

cc: Parties of Record

519165

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION



In the Matter of:

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| THE REVIEW OF BELLSOUTH TELECOMMUNICATIONS, INC.'S PRICE REGULATION PLAN | ) ) ) | CASE NO. 2003-00304 |

BELLSOUTH TELECOMMUNICATIONS, INC.'S RESPONSE TO COMMENTS OF AT&T OF THE SOUTH CENTRAL STATES, LLC, MCI WORLDCOM COMMUNICATIONS,INC. AND THE KENTUCKY ATTORNEY GENERAL

BellSouth Telecommunications, Inc. ("BellSouth"), by counsel, hereby responds to the Comments of AT&T of the South Central States, LLC ("AT&T"), MCI Worldcom Communications, Inc. ("MCI"), and the Kentucky Attorney General's office ("Attorney General"). Although the alleged concerns raised in these Comments for the most part are not pertinent to BellSouth's renewal of its existing Transition Regulation Plan ("TRP" or the "Plan"), BellSouth believes this Response may be of assistance to the Commission and therefore requests the Commission to allow its filing.

## PROCEDURAL BACKGROUND

On August 1, 2003, BellSouth filed information with the Commission regarding the three year review of BellSouth's Transition Regulation Plan. This Commission issued an order of August 14, 2003, establishing this case and setting out certain procedural requirements. The Commission also ordered, by Order dated August 25, 2003, that BellSouth's proposed tariff be suspended for five months from September 1, 2003, up to and including January 31, 2004. By Order of September 12, 2003, the

Commission required BellSouth to file its plan for elimination of band zone charges. BellSouth complied with the Commission's Order by a filing of October 3, 2003. Subsequently, AT&T, MCI and the Attorney General's Office filed comments regarding BellSouth's TRP, to which BellSouth hereby responds.

## ARGUMENT

1. The TRP Has Met Its Objectives and Should be Continued.

As BellSouth noted in its initial filing in this case, the Transition Regulation Plan has met the objectives set for it when it was adopted three years ago. This regulatory framework continues to be an appropriate plan for alternative regulation for BellSouth as the industry moves toward deregulation. As the Commission is well aware, there currently is an audit, initiated by the Commission, as a part of the process for review of the Transition Regulation Plan, to consider whether the Plan has met its objectives. The only specific change BellSouth proposed in its filing was elimination of the three year reference in the existing tariff. At the Commission's request, as noted, BellSouth filed revised pages in the General Subscriber Services Tariff to propose a plan for the elimination of zone charges over a three year period. This proposal indicated the reductions were to be accompanied by corresponding increases to replace the revenue which will be lost by elimination of zone charges.

2. Intrastate Switched Access Charges Appropriately Mirror Interstate Access Charges and Are Not Relevant to this Proceeding.

The Commission should not allow its review of the success of BellSouth's Transition Regulation Plan and BellSouth's request to continue the Plan to be sidetracked by digressions into extraneous issues, such as Intrastate Switched Access

Charges. AT&T and MCI's comments not only are self-serving and not particularly original, but they are not even relevant to the issues in this proceeding. Both of these CLECs have raised misguided concerns over the level of intrastate switched access charges in an attempt to derail consideration of the relevant issues, that is, has the TRP met its objectives. The Commission should recognize that AT&T and MCI's Comments are the "continuing mantra" set forth by those Companies in almost every forum available and often without regard to the actual purpose of the proceeding at hand. This docket concerns the renewal of BellSouth's TRP. Both AT&T and MCI would have the Commission believe that this proceeding should be expanded to provide protection for IXC business plans and the creation of new TELRIC-based UNEs for interexchange carriers. However, even if the Commission were to accept AT&T and MCI's urging to review access rates, this is not the proper proceeding for such a review. Development of such "new UNEs" has nothing to do with the provision of local retail service by a CLEC, nor is consideration of such "new UNEs" necessary or appropriate to promote competition in the local exchange market. Competition exists today. Extensive documentation of that fact has been provided in this and other proceedings.[1]

The failure to create such "new UNEs" has not resulted in diminished competition in the interexchange toll market as that market also is flush with competition. There is only one reason for AT&T's and MCI's desire for TELRIC-based IXC UNEs. That reason is not "public interest," but the desire to increase the profits of those companies.

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[1] Letter from Joan Coleman to Thomas M. Dorman and Exhibits 3-8, *In the Matter of: The Review of BellSouth Telecommunications, Inc.'s, Price Regulation Plan,* August 1, 2003. at 2, 8-10; BellSouth's Motion for Reconsideration, *In the Matter of: Petition of BellSouth Telecommunications, Inc., for Presumptive Validity of Tariff Filings,* May 22, 2003; Testimony of John A. Ruscilli and Exhibits, *In the Matter of: Petition of BellSouth Telecommunications, Inc., for Presumptive Validity of Tariff Filings,* August 22, 2003, at 5-16.

AT&T is attempting to persuade the Commission that removal of subsidies in access charges should be paramount in the implementation of the TRP.

> "Nowhere is the problem of rate subsidization more acute than in the market for access services."

See, AT&T Comments at 6.

And later on the same page AT&T proclaims:

> "The need for cost-based access rates is especially urgent now that BellSouth, in a short period of time, has proved to be highly successful in the market for interexchange services. As the monopoly supplier of access, BellSouth avoids this cost but imposes inflated charges upon its competitors. Commission action is needed to eliminate this disparity that harms AT&T and other BellSouth competitors..."

Likewise MCI alleges:

> "This matter is now of critical importance due to BellSouth's entry into the interLATA market because it is able to levy above-cost inter-carrier compensation charges on competitors, while enjoying cost-based access itself and retail pricing flexibility, as described above."

See MCI comments at 2.

The realities of the competitive marketplace and the actual positions taken by these commentors belie such rhetoric. BellSouth Telecommunications, Inc. enjoys no competitive advantage and could reasonably argue it is at a disadvantage as a result of its position in the marketplace. Intrastate-switched access is a component of interLATA toll which is a service that BellSouth Telecommunications, Inc. is prohibited from providing. BellSouth Long Distance, Inc. (BSLD), the 272 affiliate of BellSouth Telecommunications Inc., is the provider of interLATA long distance, a fact of which AT&T and MCI are well aware since they steadfastly fought the approval of BellSouth's

petition for 271 authority before this Commission. BSLD purchases switched access from BellSouth Telecommunication, Inc., on the same terms and conditions as AT&T, MCI and any other IXC.

BST and BSLD are required by law to have transactions such as these reduced to writing and open for public inspections. These transactions are posted on the BellSouth Public Policy web page. Further, BST and BLSD are subject to the non-structural safeguards and accounting requirements of FCC 96-149 and 96-150, both of which outline in explicit detail the relationship between the two companies. Likewise BellSouth is subject to the biennial audit requirements of the 1996 Telecommunications Act which examines the relationships between BST and its affiliates. There is no opportunity for BellSouth Telecommunications to place its 272 affiliate in a position superior to any other IXC in the marketplace with respect to switched access charges. The FCC made a similar finding in its Access Charge Reform Order CC Docket No. 96-262:

> "We conclude that, although an incumbent LEC's control of exchange and exchange access facilities may give it the incentive and ability to engage in a price squeeze, there are adequate safeguards in place to prevent such action." (¶ 278)

Further, BellSouth Telecommunications is not the bottleneck provider of switched access. CLECs can purchase their own switch and provide service directly to their customers and either collect access charges from the end user's IXC or bypass access charges altogether if they are both the CLEC and the IXC. In addition, CLECs can purchase UNE-P and again either collect access charges from the end user's IXC or bypass access charges altogether if they are both the CLEC and the IXC. Ironically,

neither of these options is open to BellSouth Telecommunications. An even further irony is that while AT&T and MCI want access charge relief because of toll competition from BellSouth, neither CLEC has carrier of last resort obligations to provide local exchange service to all customers in the Commonwealth. Instead, each of these CLECs can pick and choose its customers and pick and choose the method of delivering service. This freedom enables CLECs, but not BellSouth, to collect access charges.

BellSouth's intrastate-switched access rates mirror the interstate-switched access rates in BellSouth's FCC tariffs.[2] The FCC rates at their current level are a result of the CALLs proceeding to which AT&T was a participant, and the previous Access Reform proceeding in which both CLECs were participants. In those proceedings, these CLECs proposed that access charges should be at cost, ignoring the subsidy that those services provide to below cost services typically enjoyed by consumers. The FCC rejected such arguments in those proceedings. In the Access Charge Reform Order, the FCC chose not to prescribe TSLRIC-based access rates, but instead adopted a market-based access reform approach to ensure just and reasonable rates, with continued price cap regulation of services not subject to substantial competition and with a prescriptive backstop if competition in the access market did not develop as expected. (¶ 289-290)

[2] The reasonableness of BellSouth's intrastate-switched access rates in Kentucky is apparent if even a cursory comparison is made to other states in BellSouth's nine state region and the other access rates in Kentucky.

When the FCC adopted the CALLS Order, it did so in part to remove implicit subsidies from access rates. In paragraph 36 of the CALLS Order, the FCC stated:

> "We approve and adopt the CALLS Proposal because it resolves in a manner consistent with the public interest a number of complex, contentious and interrelated issues that stand as a roadblock to a competitive marketplace. The CALLS Proposal is a reasonable approach for moving toward the Commission's goals of using competition to bring about cost-based rates, and removing implicit subsidies without jeopardizing universal service."

However, Access Charge Reform apparently is not enough. MCI and AT&T are not satisfied with the CALLs Order under which the industry is operating. It appears now, these parties are engaging in forum shopping in hopes of driving intrastate-switched access charges lower than interstate. The motives for such a proposal are made clearer when the history of interstate and intrastate access charges by this Commission is examined. This Commission has been a proponent of mirroring access charges. In fact, in its order in Case No. 94-121 *Application of BellSouth Telecommunications, Inc. D/B/A South Central Bell Telephone Company to Modify its Method of Regulation* this Commission gave a persuasive rationale for its methodology.

> The Commission has generally encouraged mirroring interstate switched and special access charges. There is no evidence that the cost of interstate and intrastate access services are substantially different. Also, mirroring tends to discourage "tariff shopping" by an interexchange carrier which subscribes to the least expensive tariff, irrespective of its actual jurisdictional usage."(emphasis added).

It should be further noted that the FCC has an open proceeding that is addressing whether a uniform intercarrier compensation system would address the myriad of issues involving the differences between carrier-to-carrier compensation applicable for all types of traffic. MCI's suggestion to consider intercarrier compensation

in this price regulation proceeding is further inappropriate since that matter is under consideration by the FCC in CC Docket No. 01-92 and will be addressed there.

The allegations sets forth by AT&T and MCI in this proceeding are baseless. Their claims have been heard and rejected before in other jurisdictions.[3] There is no advantage to BellSouth in the competitive marketplace. BellSouth has requirements and obligations that no other provider in the market bears. There is no roadblock to competition as indeed this Commission has determined that Kentucky is open to competition.[4] There is no potential for BellSouth to give itself or its affiliates an advantage. There are volumes of regulations placed upon BellSouth's operations at the state and federal level. The Commission should not grant AT&T and MCI's disingenuous plea and create another arbitrage opportunity for IXC's to tariff shop. As this Commission has recognized, carriers will have a tendency to abuse such an opportunity. Further, such a grant will not further competition in either the local market, the toll market, or any other market in the Commonwealth. Finally, intercarrier compensation is being considered in an existing proceeding at the FCC and this issue should not be addressed in a duplicative state proceeding. The request of AT&T and

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[3] (1) See the FCC's Order No. 02-260 in WC Docket No. 02-150, approving BellSouth's application for In-Region, InterLATA Services in Alabama, Kentucky, Mississippi, North Carolina and South Carolina: "[T]he Commission declines to reevaluate our earlier finding that checklist compliance does not encompass the provision of tariffed interstate access services." (¶212) (2) FCC Access Charge Reform Order in CC Docket No. 96-262, ¶278. (3) On December 17, 2003, in Louisiana Docket U-24802-Subdocket B, *In re: Extension of BellSouth's Consumer Price Protection Plan,* in rendering its decision, the Commission declined to address switched access reductions as requested in MCI's pleading of October 21, 2003. ]

[4] Advisory Opinion, *In the Matter of: Investigation Concerning the Propriety of InterLATA Services by BellSouth Telecommunications, Inc., Pursuant to the Telecommunications Act of 1996,* April 26, 2002, at 5-6, 41. Amendment to Advisory Opinion, *In the Matter of Investigation Concerning the Propriety of InterLATA Services by BellSouth Telecommunications, Inc., Pursuant to the Telecommunications Act of 1996,* May 24, 2002.

MCI to expand BellSouth's TRP renewal into wholly extraneous issues should be denied.

3. The Proposed Removal of Zone Charges Over Three Years Should Be Accompanied by Corresponding Revenue Replacement.

The Attorney General correctly notes that BellSouth's proposal dealing with the removal of zone charges does not eliminate the charges, but transfers the charges from band zone rates to basic exchange rates. BellSouth does not state, nor did it intend to give the impression that it was requesting the elimination of zone charges without replacing those reduced revenues through other services' prices. The first two sentences of BellSouth's proposal attempted to make that point clear. "BellSouth proposes a gradual elimination of zone charges over a three-year period. The reductions in zone charge revenue will be offset by corresponding increases in residence and business local exchange rates and residence Local Measured Service rates."

The TRP represents a compact between BellSouth and this Commission wherein both parties have roles and responsibilities. BellSouth accepted its responsibilities and complied with the terms and conditions of the Plan. Importantly, there is no provision in the TRP requiring BellSouth to involuntarily reduce prices for services, nor is there a provision that prevents BellSouth from recovering a voluntary reduction in one service's price through increases in another. It not only is inappropriate, but also would be wholly unfair, to require a price-regulated company to eliminate a source of revenue with no

opportunity to replace that revenue through other means. BellSouth's proposal with respect to Band Zone Charges also is consistent with previous Commission orders.[5]

It is instructive to look to the Commission's July 1995 Order adopting the original Price Regulation Plan. The Commission ordered revenue reductions in the amount of $28.9M, which included zone charge reductions of $8.8M. These revenue reductions ordered by the Commission were not ordered in a vacuum, but were based on a final assessment of the appropriate revenue requirements under the former incentive sharing plan. This final review of revenue requirements formed a finishing point for former earnings-based regulation and a starting point for price regulation. Beyond that point, regulation of prices replaced revenue requirements. Any reduction in revenues, voluntary or otherwise, now comes at the expense of BellSouth's shareholders. Therefore, any future adjustment to prices should be at the discretion of BellSouth so long as such adjustments do not violate the terms of the TRP.

BellSouth's proposal here to eliminate zone charges over a three-year period and recover the lost revenues by increasing residential and business local exchange rates not only is reasonable, but also is consistent with the terms of the original Price Regulation Plan adopted in July 1995. In its July 1995 Order, this Commission considered reductions in zone charges "a high priority". As such, the Commission ordered that zones charges for bands 4 and 5 be consolidated with band 3, thereby

[5] *See* Order of July 9, 2003, *In the Matter of: Kathleen M. James, Complainant v. BellSouth Telecommunications, Inc., Defendant, Case No. 2002-00421.* The Commission, finding Band Zone Charges to be reasonable and properly approved, nevertheless, "applauded" BellSouth's suggestion to analyze those charges to see if they could be further reduced or eliminated "in a manner that harms neither customers not BellSouth". *Id.* at 2-3.

reducing charges for areas farthest from the central office. BellSouth's proposal continues to reduce the zone charges and fully eliminates them after three years.

The Attorney General suggests that zone charges are like a toll road and "were established to help cover charges for building structures so areas outside the urban areas could receive service".[6] The analogy of zone charges to charging a toll to pay for a road has some merit. Zone charges help to defray the additional cost to place facilities in areas farthest removed from the central office. However, there are ongoing costs associated with maintaining longer loop facilities. In addition, as facilities age or need to be augmented, BellSouth must continue to incur the cost to place new facilities. Therefore, just because zone charges are eliminated, the expenses associated with these longer facilities are not eliminated. As such, BellSouth rightfully should be permitted to recover lost revenue associated with eliminating zone charges through increases in basic service rates.

## CONCLUSION

BellSouth has not sought any sweeping changes in this proceeding. Rather, BellSouth sought merely to remove the three-year limitation on the Transition Regulation Plan. At the Commission's request, BellSouth also filed its plan for gradual elimination of zone charges. Of course, as BellSouth made clear in its filing, BellSouth's proposal was to offset the reductions in revenue from elimination of zone charges by corresponding increases in other appropriate rates. In a price regulation plan, it would

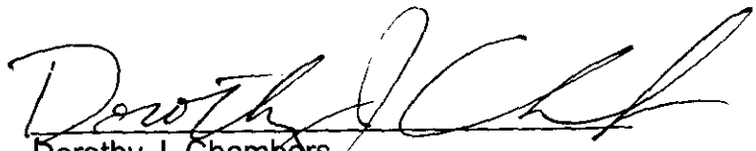
[6] Comments of The Office of the Attorney General to BellSouth's Proposed Modification to its Price Regulation Plan, *In the Matter of: The Review of BellSouth Telecommunications, Inc.'s, Price Regulation Plan,* October 13, 2003, at 2.

be inappropriate to involuntarily require BellSouth to reduce prices for services without a corresponding increase.

The only other issues raised in this proceeding were the self-serving and spurious issues raised by AT&T and MCI. Those alleged "issues" are no basis to undertake further review or examination of the proposed continuation of BellSouth's Transition Regulation Plan. The Plan has met its objectives and has provided a flexible framework to respond to changes in Kentucky's telecommunications market as the industry moves toward deregulation. Continuation of this Plan should be approved so that BellSouth can continue to respond to customer needs and to competition.

Accordingly, BellSouth respectfully requests that this Commission approve BellSouth's Transition Regulation Plan on a continuing basis as proposed in BellSouth's filings herein.

Respectfully submitted,



Dorothy J. Chambers
601 W. Chestnut Street, Room 407
P. O. Box 32410
Louisville, KY 40232
Tel. (502) 582-8219
Fax (502) 582-1573

J. Phillip Carver
Suite 4300, BellSouth Center
675 W. Peachtree Street, N.E.
Atlanta, GA 30375
Tel. (404) 335-0710

COUNSEL FOR BELLSOUTH
TELECOMMUNICATIONS, INC.

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## CERTIFICATE OF SERVICE

It is hereby certified that a true and correct copy of the foregoing was served on the individuals on the attached service list by mailing a copy thereof, this 22nd day of December, 2003.

Dorothy J. Chambers

# SERVICE LIST – PSC 2003-00304

Hon. Ann Cheuvront
Assistant Attorney General
1024 Capital Center Drive
Frankfort, KY 40601 8204

Hon. Martha M. Ross-Bain
AT&T Communications
Suite 8100
1200 Peachtree Street, N.E.
Atlanta, GA 30309

Hon. C. Kent Hatfield
Hon. Douglas F. Brent
Stoll, Keenon & Park, LLP
2650 Aegon Center, 400 W. Market St.
Louisville, KY 40202

Hon. Susan Berlin
MCI Telecommunications Corp.
6 Concourse Parkway, Suite 3200
Atlanta, GA 30328

William Atkinson, Esq.
Sprint Communications Co., L.P.
3065 Cumberland Blvd.
Mailstop GAATLD0602
Atlanta, GA 30339

Hon. John N. Hughes
Attorney at Law
124 W. Todd St.
Frankfort, KY 40601

DeMara Madison
Regulatory Compliance Coordinator
Cable & Wireless USA, Inc.
8219 Leesburg Pike
Vienna, VA 22182

Mark Romito
Cincinnati Bell Telephone Co.
201 E. 4th Street
P.O. Box 2301
Cincinnati, OH 45201-2301

Amy Hartzler
ICG Telecom Group, Inc.
P. O. Box 6742
161 Inverness Drive, West
Englewood, CO 80112

Larry Barnes
Director of Regulatory Affairs
IXC Communications Svcs., Inc.
1122 Capital of Texas Hwy. South
Austin, TX 78746

Carol P. Kihnow
Regional Director, Policy & Law
Qwest Services Corp.
5th floor
4250 North Fairfax Drive
Arlington, VA 22203

Darrell Maynard, President
Southeast Telephone, LTD
106 Power Drive
Pikeville, KY 41502 4150

Kristi Shaw
Regulatory Analyst
Teltrust Communications Services
401 N. 5600 W.
Salt Lake City, UT 84116-3753

Walter P. Drabinski, President
Vantage Consulting, Inc.
22814 Overseas Highway
Cudjoe Key, FL 33042

Mr. Stephen R. Byars
ALLTEL Kentucky, Inc.
P. O. Box 1650
Lexington, KY 40588-1650

Jonathan N. Amlung
1000 Republic Building
429 W. Muhammad Ali Boulevard
Louisville, KY 40202

Honorable Richard M. Breen
2950 Breckenridge Lane, Suite 3
Louisville, KY 40220

Charles (Gene) Watkins, Esq.
Senior Counsel
Covad Communications Company
1230 Peachtree Street, NE, 19th Floor
Atlanta, GA 30309